



**RICHARD ECKSTROM**  
COMPTROLLER GENERAL

State of South Carolina  
**Office of Comptroller General**

1200 Senate Street  
305 Wade Hampton Office Building  
Columbia, South Carolina 29201

Telephone: (803) 734-2121  
Fax: (803) 734-2064  
E-Mail: [cgooffice@cg.state.sc.us](mailto:cgooffice@cg.state.sc.us)

**NATHAN KAMINSKI, JR.**  
CHIEF OF STAFF

December 29, 2003

**To the Citizens, Governor and  
Members of the South  
Carolina General Assembly**

I am pleased to present to the citizens of South Carolina this Comprehensive Annual Financial Report for the State of South Carolina for the fiscal year ended June 30, 2003. The report provides financial information about the State's operations during the year and describes its financial position at the end of the year.

Management is responsible for the accuracy of the data in this report as well as for the completeness and fairness of the presentation. To the best of our knowledge and belief, this information is accurate in all material respects and is reported in a manner that presents fairly the State's financial position and results of operations and provides disclosures that enable the reader to understand the State's financial condition. For the convenience of users, we have divided the report into three sections as follows:

- The Introductory Section, containing this letter of transmittal; the Certificate of Achievement for Excellence in Financial Reporting for the report as of June 30, 2002; a list of State officials; and an organizational chart of State government.
- The Financial Section, including the independent auditors' report, management's discussion and analysis, government-wide financial statements, fund financial statements, required supplementary information, other combining financial statements, and schedules.
- The Statistical Section, presenting comparative financial data and other non-financial data.

This letter of transmittal is designed to complement management's discussion and analysis that immediately follows the report of the independent auditors.

**PROFILE OF THE STATE OF SOUTH CAROLINA**

South Carolina stretches from the Atlantic Ocean to the Blue Ridge Mountains, containing 30,111 square miles. The coastal area, which is one of the leading recreation centers on the east coast, is the anchor of the State's thriving tourism industry. Since 1970, over 740,000 people have relocated to South Carolina to take advantage of its growing economy and to retire here.

As shown in the organization chart on page 15, South Carolina's government is divided into three separate branches: legislative, executive, and judicial. State government provides a full range of services to South Carolina's citizens including educational, health, social/human, transportation, public safety, regulatory, and conservation/natural resources services. In addition, the State provides grants and loans to local governments, including school districts, within its borders.

South Carolina is primarily a manufacturing state. While the textile industry is still the major industrial employer in the State, the State's economy has undergone a gradual transition to other sectors. Since 1950, the State's economic base has diversified into other sectors such as trade, health care, services, and durable goods manufacturing.

## **BUDGETARY AND INTERNAL CONTROLS**

The Statewide Accounting and Reporting System (STARS) is the State's budgetary-basis operating accounting system. The STARS system processes cash and budgetary transactions and maintains records for all budgeted funds and some unbudgeted funds. The State's higher education institutions and most of the other enterprise entities maintain separate accrual-basis accounting systems.

The Comptroller General's Office maintains an automated annual financial reporting system as well as an automated interface between STARS and that system. The Comptroller General's Office uses this automated system and interface to prepare this report in accordance with generally accepted accounting principles (GAAP). State agencies that use STARS prepare year-end forms to report amounts needed to adjust their budgetary-basis balances to comply with GAAP. The Comptroller General's Office then enters the data from these forms into its GAAP financial reporting system. Additional information entered into the GAAP financial reporting system is derived from the audited financial statements of certain entities and from other supplemental data provided by those entities.

South Carolina's annual Appropriation Act includes legally adopted budgets for the Budgetary General Fund and for Total Funds. For additional information, see the notes to the required supplementary information—budgetary. The initial budget appears in the annual Appropriation Act. After the budget year begins, the State Budget and Control Board may order spending cuts if revenue collections fail to reach predicted levels.

The State's internal controls, designed by the management of the State, provide reasonable assurance that the State will achieve the following objectives:

- Reliability of financial reporting,
- Effectiveness and efficiency of operations, and
- Compliance with applicable laws and regulations.

The concept of reasonable assurance recognizes that the cost of a control should not exceed the resulting benefits.

## **MAJOR INITIATIVES**

The General Assembly spent much of its 2003 session addressing concerns regarding the State's 2003-2004 budget. However, it also passed some major agency restructuring bills that reorganized the State's motor vehicle functions and its homeland security duties.

In order to improve agency accountability and provide to the public more cost efficient and effective services, the General Assembly, through the Department of Motor Vehicles Reform Act of 2003, carved from the Department of Public Safety two discrete units: the motor vehicle division and the motor carrier services unit. These units were moved under the supervision of the newly created Department of Motor Vehicles, established by the Act as a separate administrative agency, with a director appointed by, and directly accountable to, the Governor.

The homeland security legislation assigned most homeland security functions to the State Law Enforcement Division (SLED). Under the new law, SLED may establish and operate tactical response law enforcement units, coordinate counter-terrorism efforts in or affecting South Carolina, coordinate

federal homeland security grants, and represent the Governor in dealing with the United States Department of Homeland Security.

In a related effort, the South Carolina Maritime Security Act created the Maritime Security Commission. It also reestablished the South Carolina Naval Militia to augment port and coastal security.

Among other legislative actions, the General Assembly during the 2003 session strengthened laws for dealing with DUI offenders, domestic violence offenders, and predatory lending practices.

## **ECONOMIC CONDITION AND OUTLOOK**

Over the last three decades, South Carolina's economy has grown, and continues to grow, faster than that of the rest of the country. Businesses have migrated here from all over the world to take advantage of the State's skilled labor force, competitive wages, lower-priced land, excellent port facilities, accessibility to markets, and in recent years, substantial tax incentives.

Several global companies have located corporate headquarters or multi-million-dollar manufacturing facilities within South Carolina. BMW recently announced that it plans to invest an additional \$400 million in its Upstate factory, creating 400 more jobs. In addition to BMW, other newly announced plants and expansions of existing facilities are expected to contribute to South Carolina's continued economic growth.

An impressive influx of people into South Carolina over the last three decades has generated tremendous economic growth in the State's coastal regions. These areas continue to distinguish themselves as leading tourist, recreation, and retirement centers relative to the entire United States East Coast. The growth along the coast has contributed significantly to the burgeoning economy of the State as a whole.

Since 1970, total South Carolina personal income increased over 1,200 percent and grew 20 percent faster than total United States personal income through 2000. During this period, 1970's personal income grew at an average annual compound rate of 11.9 percent in South Carolina (compared to 10.7 percent nationwide). During the 1980's, the State's personal income grew 8.7 percent per year (compared to 7.8 percent nationwide). Even in the 1990's, when inflation was lower, personal income in South Carolina grew a healthy 5.7 percent per year (compared to 5.6 percent nationwide). Despite the recent recession, South Carolina's total personal income still managed to grow 20 percent faster than the rest of the country.

Between 1970 and 2000, employment in South Carolina grew approximately 40 percent faster than in the United States as a whole. Despite the recent slowdown in the economy, employment levels in South Carolina have continued to fare better than in the nation as a whole. In fact, South Carolina had at least 246,000 jobs more in September 2003 than it had during the recession of 1991. See the management's discussion and analysis section of this report for additional information on the State's economy.

## **LONG TERM FINANCIAL PLANNING**

In June 2003, Governor Mark Sanford issued an executive order establishing the Governor's Commission on Management, Accountability and Performance (the MAP Commission). This fourteen-member Commission, comprised of prominent business leaders and state officials, was charged with the responsibility of analyzing government systems and services in South Carolina and was directed to propose changes to "reduce costs, increase accountability, improve service, consolidate similar functions, return functions to the private sector, and help South Carolina be more competitive in a world economy."

The MAP Commission issued a comprehensive report on September 30, 2003, which can be found on the Internet at [www.state.sc.us/governor](http://www.state.sc.us/governor). The report recommended sweeping changes for the structure of state government and focused on a number of areas dealing with its fiscal management.

Among some of the MAP Commission recommendations are proposals to increase the accuracy and reliability of revenue forecasting upon which the state appropriations act is based each year; increase the Constitutionally-established set-aside for capital and nonrecurring purposes from 2% to 3%; discontinue the practice of funding recurring expenses with non-recurring revenues; adopt a performance-based budgeting process instead of the current practice of incremental budgeting; and gradually eliminate the mismatch in revenues and expenditures resulting from using a “13th month” accrual of selected revenues.

The MAP Commission also recommended implementing a statewide capital budgeting process that would improve the current multi-year planning process contained in the State Comprehensive Permanent Improvement Plan by establishing a Capital Budgeting Authority to analyze and screen capital projects planned over the next three to five years and establishing a separate maintenance budget. Many of these recommendations will require authorization by the General Assembly and, in some cases, amendments to the State Constitution. It is expected that many of the recommendations included in the MAP Commission report will be reviewed and considered in the 2004 session of the General Assembly.

## **FIDUCIARY OPERATIONS**

The most significant of the State’s fiduciary funds are the four retirement plans administered by the South Carolina Retirement Systems. Those plans include: the South Carolina Retirement System, the Police Officers’ Retirement System, the Retirement System for Members of the General Assembly, and the Retirement System for Judges and Solicitors. The State has funded all four of those plans in accordance with at least the minimum recommendations of the consulting actuaries, both in the current period and in past periods. See Note 9, Retirement Plans, in the notes to the financial statements for more information.

## **CASH MANAGEMENT**

The State Treasurer is responsible for managing the State’s cash and investments, except for certain component units included within the reporting entity that manage and invest their own funds. State law requires full collateralization of all State Treasurer bank balances. Some component units may have collateralization policies that differ from those of the State Treasurer.

Investment income includes appreciation and depreciation in the fair value of investments. Increases in fair value during the current year, however, do not necessarily represent trends that will continue; nor is it always possible to realize such amounts, particularly in the case of temporary changes in the fair value of investments that the State plans to hold to maturity. For additional details, see Note 1f, Summary of Significant Accounting Policies, and Note 5, Deposits and Investments, in the notes to the financial statements.

## **RISK MANAGEMENT**

The State conducts various risk control programs to help minimize losses to which it is exposed. The health insurance program conducts extensive wellness education programs that promote development and maintenance of healthful lifestyles for covered employees. The State self-funds many types of general liability and property losses rather than purchasing insurance. For additional information on the State’s risk management activities, see Note 11, Insurance Activities, in the notes to the financial statements.

## AUDIT

The State Auditor and KPMG LLP, an independent certified public accounting firm, jointly performed an independent audit of the State's basic financial statements for the fiscal year ended June 30, 2003. The auditors have provided an unqualified opinion, the most favorable outcome of the audit process.

## CERTIFICATE OF ACHIEVEMENT

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the State of South Carolina for its comprehensive annual financial report (CAFR) for the fiscal year ended June 30, 2002. To receive a Certificate of Achievement, which is valid for one year only, a government must publish an easily readable and efficiently organized CAFR. The CAFR contents must conform to rigorous program standards, including generally accepted accounting principles and applicable legal requirements. The State of South Carolina has received a Certificate of Achievement for the last fifteen consecutive years. This year, the State again plans to submit its CAFR to the GFOA's Certificate of Achievement program. We believe that South Carolina's report for the fiscal year ended June 30, 2003, continues to meet the requirements to receive the Certificate of Achievement.

## ACKNOWLEDGMENTS

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Sincerely,



Richard Eckstrom  
Comptroller General